Finance director's report

2022 was an eventful year marked by strong demand, ongoing problem-solving of supply chain challenges and product cost pressures driven by global demand, high inflation and exchange rate volatility.

Although the financial returns for 2022 are not yet at the targeted level, the business has made strides in the right direction and we look forward to further improvement in 2023.

Financial Performance

Revenue of R10,3 billion for 2022 was 28,2% up on 2021 sales of R8,0 billion. The first half of the year was constrained by component shortages at the factories which impacted production and sales volumes, but the supply chain was more reliable in the second half of the year and this facilitated the catch up of production and improved delivery of machines and invoicing to customers before year end. Revenue for the second half of the year was 43,0% up on the first half of the year. This also had a positive impact on inventory levels and borrowings and we are satisfied with where these levels ended the year, especially considering the gearing up of the production schedule for higher demand in 2023.

The group earned a profit after tax of R478,9 million for the year, 62,7% up on R294,3 million earned for the 2021 financial year. The higher sales and higher production volumes at the group's two manufacturing facilities had a positive impact on the bottom line. The positive impact of the higher production volumes on the profitability of the group is evident in the improved operating results reported for the group's manufacturing operations in South Africa and Germany. Earnings per share and headline earnings per share were 478 cents and 473 cents respectively (2021: earnings per share of 300 cents and headline earnings per share of 294 cents per share) for the year. A final dividend of 90 cents per share was declared.

The company's share price is still trading at a significant discount to net asset value per share and as this is an indicator of possible impairment in terms of *IAS 36 Impairment of Assets, valuations and assessments* were performed to determine the recoverable amount of the group's main cash generating unit and certain other key assets in the group. No impairments resulted from the valuation of the cash generating unit. The usual, ongoing assessments of inventory and receivables resulted in certain provisions and allowances for expected credit losses being accounted for. Refer to note 5 in the annual financial statements for further details of this assessment.

Segmental performance

There was no change to the group's two main business operations in 2022. The group still conducts OEM operations comprising manufacturing, assembly and sales of equipment and aftermarket products to independent and group owned distributors and dealers. These OEM operations are conducted from South Africa and Europe. The second business is the direct sales business which comprises owned distribution operations in South Africa and Rest of Africa that are engaged in direct sales of own manufactured products, other third party products and the supply of aftermarket support and products to the market. The South Africa direct sales business comprises customer service centres in South Africa and Eswatini. Rest of Africa comprises customer service centres in Zambia and Zimbabwe.

The OEM business in South Africa reported a significantly improved operating profit of R369,2 million in 2022, up from R8,6 million in 2021. This segment's result is sensitive to volumes and the improvement in result was due to higher production and sales volumes in 2022. Higher sales of complete machines to customers in the southern hemisphere and higher sales of kits to the German factory for completion of ADTs destined for the USA, UK and Europe, contributed to a higher recovery of overheads at the Richards Bay facility compared with 2021. Total sales, including both external and inter-segment sales, increased by 37,2% in 2022. External revenue contributed 19,8% of group sales in 2022 compared with 19,4% in 2021.

External sales by the OEM business in Europe increased by 21,5% with the contribution to total group sales reducing from 38,4% in 2021 to 36,4% in 2022. Although volumes sold in the USA and UK were up on 2021 volumes, operating profit reduced from R157,6 million in 2021 to R141,8 million in 2022. Margins were under pressure due to high inflation and product cost increases that were initially absorbed by the operations while orders were fulfilled at selling prices committed to in earlier periods. Much of the increase in demand was driven by government-initiated infrastructure development programmes and restocking programmes which are expected to continue in 2023. The Russian business remains on pause due to the war in Ukraine.

External revenue from direct sales operations in South Africa increased by a pleasing 29,0% compared with 2021 and the contribution to group sales increased marginally to 38,2% in 2022, compared with 38,0% in 2021. The South African sales operation exceeded expectations in 2022, mostly driven by mining activity, and reported operating profit of R175,0 million up from R94,0 million in 2021.

The external sales of the owned customer service centres in Zambia and Zimbabwe, which comprise the group's Rest of Africa operations, experienced strong growth in 2022 especially in Zambia and increased by 71,4% on 2021. This however remains a small part of the business, contributing 5,6% to group sales in 2022. The group continues to support customers in difficult conditions in Zimbabwe on the basis of payment in advance in South Africa for parts and machines supplied.

Gross Margin
The gross margin is dependent on the product and geographic mix of sales, market conditions and exchange rates. Input costs continued to rise sharply in 2022 affecting component and raw materials prices and logistics costs. The US Dollar strengthened against both the Euro and the Rand and this was generally favourable for the group, being a net earner of US Dollars, however the significant currency volatility experienced in 2022 was difficult to manage and together with the product cost increases, added pressure to gross margins. The average gross margin for the year was 19,8% compared with 19,3% in the prior year.

Other operating income
Other operating income relates mainly to production incentives in the form of import duty rebates earned on the South African government's Automotive Production Development Programme. This benefit increased by 58,8% to R144,4 million in 2022 from R90,9 million in 2021, due to the increase in production volumes of qualifying products in 2022.

Expenses
The weaker Rand, high inflation, higher production volumes, increases in fuel and electricity costs and a return to greater normality with regard to travel, on site customer support and international product exhibitions, resulted in overheads increasing by 19,7% in 2022. Production related variable costs, including contract labour salaries and overtime, increased due to higher production volumes in 2022.

The group has continued its investment in research and development and development costs totalling R29,9 million were capitalised during 2022. These costs are amortised over the life of new products once projects have been completed. The total cumulative carrying value of capitalised development costs at year end amounted to R225,1 million and the total amortisation of development costs for the year amounted to R30,6 million.

Interest paid
An increased investment in inventory was required for the increased demand and production volumes and to counter supply chain challenges. Borrowings were therefore at a higher level in 2022 than in the prior year. Interest paid was R137,0 million for 2022 compared to R96,4 million for 2021.

Taxation
The effective group tax rate of 25,8% is in the range expected given the statutory tax rates in the jurisdictions of the group's main operations.

Financial position
The net asset value per share increased by 13,1% from 4038 cents in 2021 to 4565 cents in 2022. This was mainly due to the profit generated in 2022, and to a lesser extent also due to an increase in the net foreign assets of the group and the foreign currency translation reserve as a result of the weaker Rand at year end compared with the 2021 year-end, as well as the gain on revaluation of the group's owned land and buildings.

Property, plant and equipment
The group's owned land and buildings were revalued in 2022 in line with the group's accounting policy. As a result of the revaluations, a revaluation surplus of R58,1 million, relating mainly to the Richards Bay properties, was accounted for in other comprehensive income. A reversal of a prior period impairment loss of R5,8 million relating to the group's property in Kitwe, Zambia, was accounted for in profit or loss.

Additions to capex of R98,9 million in 2022 comprised mainly replacement factory plant and equipment of R85,3 million.

Right-of-Use Assets and Lease Liabilities
Right-of-use assets increased by R116,9 million in 2022, relating mainly to two significant new property leases. A 7 year property lease relating to the group's manufacturing and assembly facility in Kindel, Germany, for an amount of R90,2 million was concluded and a 10 year property lease totalling R46,1 million was entered into for warehousing space in Richards Bay.

Deferred tax assets
The group has substantial deferred tax assets of R214,4 million, down from R231,6 million in 2021. The largest items included in this balance relate to the group's contract liabilities, where the proceeds from the sale of extended warranty contracts and service and maintenance contracts have been received and taxed upfront, the group's standard warranty provision where the actual warranty costs will be deductible in future periods and to the elimination of unearned profit in inventory on consolidation of the group results.

Working capital
Considering the ramp up for the stronger order book for 2023 and the supply chain challenges experienced during 2022 which had not been completely resolved and worked out of inventory by year end, we are satisfied with the 210 days inventory at year end. This is measured on historical cost of sales and compares with inventory of 204 days at the end of 2021. Inventory of components, raw materials and finished goods inventory were all higher in Rand terms at the end of 2022 compared with 2021 due to the higher level of activity and sales compared with 2021, the ramp up in production for higher sales forecast for 2023 and due to a planned increase in aftermarket parts to enhance parts availability and response times. On a forward looking basis, inventory days were substantially lower than 210 days.

Trade receivables days ended 2022 at 45 days, down from 47 days at the end of 2021. Total allowances for expected credit losses amounted to R48,9 million at year end, of which R31,9 million related to customers in the South African market. Overall, the general health of trade receivables improved in 2022 with fewer customer accounts falling into arrears during 2022. The group has experienced low bad debts in the past and even if certain customer accounts take time to collect, they are generally recovered in full.

Inventory and receivables of R390,0 million and R70,0 million respectively in the group's operation in Germany was provided as security for a new borrowings base facility implemented in 2022. This facility will assist with funding the working capital required for the 2023 production volumes and positions the group for further growth offshore.

Prepayments to suppliers for inventory purchases increased significantly in 2022 and the negotiation of stronger terms for the supply of certain components is a focus area for 2023.

Cash generated and borrowings
When the group ramps up for stronger market conditions this

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requires a cash investment in inventory. Gearing increased to 26,3% from 18,0% at the end of 2021. Although production and sales volumes are expected to increase in 2023, cash flow forecasts indicate that the group has sufficient borrowing facilities to meet its plans and cash flow requirements.

Exchange rates

As reported above, the most significant currency movement for the group in 2022 was the strengthening of the US Dollar against the Rand and the Euro. The group reported net currency gains of R24,1 million for the year, mainly arising on USD denominated receipts and receivables balances in the German subsidiary and at the Richards Bay factory. Not reflected in this net foreign currency gain is the positive impact of a weaker Rand on invoiced revenue and gross margins.

The group's approach to managing foreign currency exposures remains the same as in past years. A substantial portion of the group's purchases and sales transactions are in currencies other than the SA Rand. As far as possible we aim to match currency inflows and outflows and the group has a strong natural currency hedge. Forward cover contracts are used to assist in managing the residual currency exposures.

The group is further exposed to currency fluctuations with respect to the translation of profits into Rand, as a substantial portion of the group's operating profit is derived from operations outside South Africa.

Looking ahead

The group looks forward to further growth and improvement in the financial results in 2023. We are cautiously optimistic regarding demand from the northern hemisphere markets and concerns regarding the global economy and the supply chain which has not fully recovered will be closely monitored.